1976

Richard Madsen and Nancy A. Madsen v. Prudential Federal Savings & Loan Associations : Brief of Respondent

Utah Supreme Court

Robert J. DeBry; Attorneys for Appellants.
Joseph J. Palmer; Moyle & Draper; Attorneys for Respondents.

IN THE SUPREME COURT OF THE STATE OF UTAH

RICHARD MADSEN and NANCY A. MADSEN, his wife,

Plaintiffs-Appellants,

vs.

PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION,

Defendant-Respondent.

Case No. 14530

BRIEF OF RESPONDENT

APPEAL FROM THE JUDGMENT OF THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT IN AND FOR SALT LAKE COUNTY, STATE OF UTAH, HONORABLE BRYANT H. CROFT, DISTRICT JUDGE

Joseph J. Palmer, of
MOYLE & DRAPER
600 Deseret Plaza
Salt Lake City, Utah 84111

Attorneys for Respondents

ROBERT J. DeBRY
2040 East 4800 South, Suite 203
Salt Lake City, Utah 84117

Attorneys for Appellants

FILED

SEP 2 1976

Clerk, Supreme Court, Utah

IN THE SUPREME COURT OF THE STATE OF UTAH

RICHARD MADSEN and NANCY A. MADSEN, his wife,

Plaintiffs-Appellants,

vs.

PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION,

Defendant-Respondent.

Case No. 14530

RESPONDENT'S BRIEF OF NEWLY UNCOVERED CASES

Pursuant to Rule 75(p)(3), Utah Rules of Civil Procedure, respondent submits the attached pages of newly uncovered cases for insertion in the brief of respondent, all cases applying to Point III of respondent's brief.

DATED this 5 day of November, 1976.

MOYLE & DRAPER

By Jos J. Palmer
Joseph J. Palmer
Attorneys for Respondent
600 Deseret Plaza
Salt Lake City, Utah 84111

Brooks v. Valley National Bank (Sup.Ct. of Ariz., April, 1976), 548 P.2d 1166 ("Brooks II"), supersedes the opinion of the Arizona Court of Appeals in Brooks v. Valley National Bank, 539 P.2d 958 (1975) ("Brooks I"), cited at page 31 of respondent's brief. Brooks II sustained the Superior Court's granting of motion to dismiss the action, as did Brooks I, holding: (a) a trust was not created for the impounded funds even though the words "in trust" were used in the mortgage documents, and (b) the bank was not unjustly enriched through use of the funds. The reasoning follows the opinion in Brooks I cited in respondent's brief. The concurring opinion in Brooks II reasoned that a trust was created because the bank received the funds to be applied to a particular purpose but, nevertheless, the dismissal of the complaint was still proper, saying:

> Brooks relies on the general rule of law that it is the duty of a trustee to protect the interests of the beneficiary of a trust by the exercise of reasonable care and diligence in the management of the trust property, Bulla v. Valley National Bank of Phoenix, 82 Ariz. 84, 308 P.2d 932 (1957), and the general rule that that trustee has a duty to invest the trust property so that it is made productive for the beneficiary. Restatement (Second) of Trusts, §181 (1959). Where, however, a rule of law might otherwise be applicable to an agreement, custom or usage may make such rule of law inapplicable. Williston, Law of Contracts, §648 (3rd ed. 1961).

> The practice of requiring impound payments has existed since the early 1930's. In every instance, without exception, where a suit has been brought to compel payment of interest or the earnings on the investment of the impound funds, the lending institution has not paid the mortgagor for the use of the impound funds. Nor is there anywhere the slightest suggestion that the Valley National Bank or any lending institution ever paid for the use of impound funds.
>
> While a few isolated instances will not prove a usage, one so firmly established for so many years nationwide should be controlling. A usage will be binding if it is uniform, long established, and so well known that it can be said that the parties contracted with reference to it and the failure to conform to it would be the exception. Cleveland etc. R.R. Co. v. Jenkins, 174 Ill 398, 51 N.E. 811. Nor is a usage invalid because its effect is different from a general rule of law.
>
>> It is well settled that a trade usage which is contrary to a statute or which contravenes public policy is invalid and may not be invoked; but where a rule of law is of a character that the parties may make it inapplicable to their contract by express agreement, they may likewise render it inapplicable by implied usage or by usage." Wolfe v. Texas Co., 83 F.2d 425, 431 (10th Cir. 1936).
>
> I am therefore of the opinion that by banking usage neither interest nor earnings on investment was expected to be credited to the mortgagor.

A not-yet-reported decision is Throp v. Bell Federal Savings & Loan Assoc., Ill.App.Ct., Docket No. 60252, decided July 26, 1976, aff'd on rehearing, 10-7-76.

It affirmed granting of defendant's motion to dismiss of plaintiff's claim for earnings on the escrow funds, saying "the use or non-use of the words 'in trust' is not the controlling criteria as to whether an express trust has or has not been created." It is the most recent decision on the subject and contains a review of recent authorities similar to other cases cited in respondent's brief. Its reasoning is applicable to appellants' simplistic argument as to use of the word "pledge" in the mortgage document.

Finally, we cite the Report of Committee on Real Estate Financing entitled "Class Actions Under Antitrust Laws on Account of Escrow and Similar Practices," Real Property Probate and Trust Journal of the American Bar Association Section of Real Property, Probate and Trust Law, Volume 11, No. 2, Summer, 1976. It concludes:

> If lenders begin to pay interest on escrow accounts, realistically the additional expenses that result will in some manner be borne by borrowers either by a carrying charge or increase in the loan rates which would cover these expenses. In short the payment of interest on escrow accounts would not result in any economic benefit to borrowers and would in all probability increase costs at least on smaller loans.

CERTIFICATE OF SERVICE

I hereby certify that on the 5th day of November, 1976, two true and correct copies of the foregoing Respondent's Brief of Newly Uncovered Cases were delivered to Robert J. DeBry, attorney for plaintiffs, 2040 East 4800 South, Salt Lake City, Utah.

IN THE SUPREME COURT OF THE STATE OF UTAH

RICHARD MADSEN and NANCY A. MADSEN, his wife,	)	
	)	
Plaintiffs-Appellants,	)	Case No. 14530
vs.	)	
PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION,	)	
Defendant-Respondent.	)	

BRIEF OF RESPONDENT

APPEAL FROM THE JUDGMENT OF THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT IN AND FOR SALT LAKE COUNTY, STATE OF UTAH, HONORABLE BRYANT H. CROFT, DISTRICT JUDGE

Joseph J. Palmer, of
MOYLE & DRAPER
600 Deseret Plaza
Salt Lake City, Utah 84111

Attorneys for Respondents

ROBERT J. DeBRY
2040 East 4800 South, Suite 203
Salt Lake City, Utah 84117

Attorneys for Appellants

TABLE OF CONTENTS

CASES CITED

STATUTES CITED

REGULATIONS CITED

OTHER AUTHORITIES CITED

IN THE SUPREME COURT OF THE STATE OF UTAH

RICHARD MADSEN and NANCY A. MADSEN, his wife,	)	
Plaintiffs-Appellants,	)	Case No. 14530
vs.	)	
PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION,	)	
Defendant-Respondent.	)	

BRIEF OF RESPONDENT

STATEMENT OF THE KIND OF CASE

This is a contract action. Plaintiffs, as borrowers, executed a trust deed to defendant lender in a typical residental mortgage transaction. As required by the trust deed, for 11 years plaintiffs paid defendant monthly payments of principal and interest, and a "budget payment" of 1/12 of estimated annual real property taxes and insurance premiums, without expectation of receiving any compensation on the budget payments. Although the contract is silent on the subject, plaintiffs now complain that defendant should pay plaintiffs the net earnings on such budget payments on a theory of unjust enrichment.

DISPOSITION IN LOWER COURT

The Third Judicial District Court in and for Salt Lake County, the Honorable Bryant H. Croft, denied plaintiffs' motion for partial summary judgment as to liability and granted defendant's motion for summary judgment dismissing the complaint, no cause of action (R.479-80).

RELIEF SOUGHT ON APPEAL

Defendant prays the judgment be affirmed, and that it be awarded its costs on appeal.

FACTS

The facts are not in dispute. Only a few additions are necessary to plaintiffs' Statement of Facts.

On September 21, 1964, plaintiffs, as borrowers, executed to defendant a trust deed (R.2). By paragraph 4 of the trust deed (R.5), plaintiffs promised to pay and have paid defendant, for 11 years, not only monthly payments of principal and interest, but also a monthly payment of 1/12 of estimated annual real property taxes and insurance premiums on the mortgaged property, referred to variously in the cases as "budget payments," "reserves," "impounds" or "escrows".

The interest rate on plaintiffs' loan, still unpaid, is 6-1/2 percent per annum.

The complaint sought to require defendant to pay interest or earnings on the reserves, although no provision is made for such under the contract. The complaint claimed two theories: (1) breach of contract, or (2) unjust enrichment.

Plaintiffs' complaint, paragraphs 13 through 16 (R.3) alleges the trust deed includes an "implied term" that defendant will pay reasonable interest on monies paid to it for payment of taxes and insurance, that defendant has breached the contract by not paying any interest to plaintiffs, and that defendant is liable for such unpaid interest. The claim for interest apparently has been abandoned on appeal (appellants' brief, p.1).

Paragraphs 17 through 21 of the complaint (R.3-4) set forth alternative allegations of unjust enrichment to the effect that defendant has earned a substantial profit from the use of the reserve fund "belonging to plaintiffs," thereby becoming unjustly enriched, and praying for restitution of the earnings represented by such unjust enrichment. That apparently is the only claim urged on appeal (appellants' brief, pp.1, 17-18).

The pertinent portions of the contract, the trust deed (R.5, 58-59), are paragraphs 2 and 4 (R.5). It is accurately quoted on pages 2 and 3 of plaintiffs' brief.

Plaintiffs testified on deposition that:

(1) When plaintiffs executed the trust deed they knew the trust deed required them to pay the monthly budget payments (depo., pp.9-10, 26).

(2) Plaintiffs, at execution, knew defendant would not pay plaintiffs interest or earnings on the budget payments (depo., p.26). Plaintiffs thought that unfair at the time (depo., p.47), but had no discussion with defendant's personnel as to the required budget

payments or as to payment of interest or earnings thereon (depo., p.10).

(3) Since 1964, plaintiffs have paid all such budget payments each month without expectation that defendant would pay interest or earnings on such reserves (depo., p.26), and plaintiffs have never asked for payment of earnings or that budget payments not be commingled (depo., pp.23, 25).

Defendant's affidavit states why, for 20 years, its policy has been to require the reserve payments and why it has not paid interest or earnings on them (R.282-4).

Plaintiffs admit (plaintiff's brief, p. 3) that the requirement of collection of monthly budget payments is standard or required procedure for lenders, as evidenced by the Federal regulations and state statutes quoted in their brief, pp. 3-5.

A new regulation was promulgated by the Federal Home Loan Bank Board on June 16, 1975 to prescribe the circumstances under which federal savings and loan associations, such as defendant, may pay interest on escrows. It provides (12 C.F.R., §545.6-11(c)):

> A Federal association which makes a loan on or after June 16, 1975, on the security of a single-family dwelling occupied or to be occupied by the borrower (except such a loan for which a bona fide commitment was made before that date) shall pay interest

> on any escrow account maintained in connection with such a loan (1) if there is in effect a specific statutory provision or provisions of the State in which such dwelling is located by or under the State-chartered savings and loan associations, mutual savings banks and similar institutions are generally required to pay interest on such escrow accounts, and (2) at not less than the rate required to be paid by such State-chartered institutions but not to exceed the rate being paid by the Federal association in its regular accounts (as defined in Section 526.1 of this chapter). <u>Except as provided by contract, a Federal association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph</u>. (Emphasis added.)

Utah statutes are silent as to any requirement that interest be paid on escrows; indeed the silence in the authorization statutes (§§7-7-5(e)(3) and 7-12-47(1)(2), U.C.A. 1953), is deafening.

Plaintiffs' reserve account for 1974 (Exhibit A attached to plaintiff Madsens' deposition) shows an average monthly balance of $275.47 (by adding monthly balances and dividing by 12), on which the gross earnings at, say, five percent per annum, would be $13.77 for the year before considering defendant's cost of handling the account and producing the earnings. Defendant estimated the cost would be more than $16 per account per year (R.287).

On this record, the lower court granted defendant's motion for summary judgment and denied plaintiffs' motion for partial summary judgment on liability (R.479-80). Plaintiffs filed timely appeal.

ARGUMENT

POINT I

SOCIAL CONSIDERATIONS MITIGATE AGAINST PLAINTIFFS' CLAIM

Plaintiffs' claim is controlled by the contract between the parties. Nevertheless, actions of this type have become very popular lately, as will be seen by the number of cases recently filed in other jurisdictions, all unsuccessful. The reason for the popularity is set forth in appellants' brief, pp.21-2:

> The concept of setting aside a prorata share of annual tax and insurance costs each month in a separate account arises from the experience of lenders during the depression of the 1930's, when many people lost their homes in tax foreclosures. In order to make mortgage loans more attractive to lenders, the Federal Housing Administration made escrow accounts mandatory on all FHA-insured mortgage loans. At that time, interest rates paid on savings accounts were so low -- around 1 or 2 percent -- that no thought was given to payment of interest on escrow accounts. In fact, some lenders charged an extra fee for handling the accounts. Over the years, the prepayment of tax and insurance payments into escrow accounts that bear no interest became established practice within the lending industry, not only for government-insured loans, but for conventional mortgage loans as well.
>
> But times have changed. Passbook interest rates are no longer at 1 percent. The amount of money held in savings accounts is at an all-time high and the problem of tax foreclosures today is nowhere near what it was in the 1930's. As for the escrow funds lenders hold, it has become an accepted practice for many lenders to commingle these funds

> with other money invested for profit. Thus, the lenders have become accustomed to substantial income from the investment of mortgage borrowers' escrow funds, and seldom do they share those earnings with the people who own the money.
>
> There are no national figures to show how much mortgage lenders earn from the interest-free use of escrow money, but a study by Prof. John A. Spanogle, Jr., of the University of Main School of Law, estimates it at $100 million a year. "Homeowners vs. Lenders -- A Question of Interest," 38 <u>Consumer Report</u> 202 (1973).

Plaintiffs' claim is of great significance to the entire mortgage lending industry and the Federal Home Loan Bank Board, which regulates all national savings and loan associations, including defendant. The claim also affects routine real estate contracts, where often it is expressed that the buyer's monthly payments include a reserve for taxes and insurance.

The claim of plaintiffs, if successful, would adversely affect the marketability of mortgages in the secondary market. Mortgages are sold like commodities, sometimes outright and sometimes with the seller remaining obligated to the buyer to service the loan.

In defendant's case, in August, 1975, 20,388 mortgages were on the books, of which (a) 3,749 had been sold, including reserves, to 17 different investors, including governmental investors such as Federal National Mortgage Association, Government National Mortgage Association, Federal Home Loan Mortgage Corporaton and Utah State

Retirement Fund; (b) 4,301 participation interests had been sold; and (c) 603 were purchased from other original mortgagees. About 100 mortgages are sold outright each year and are no longer on defendant's books (R.74).

The Intermountain area is and traditionally has been "savings poor," that is, the public does not make sufficient time or savings deposits to sustain the growing demand for mortgage money for new residential and commercial buildings. As a result, defendant and other lenders in this area depend upon the secondary market where they, from time to time, and not necessarily when a particular mortgage is closed, sell mortgages either outright or with participation interests to obtain necessary cash for mortgage demands. Thus, in August, 1975, defendant had sold interests in varying amounts up to 100 percent of 8,050 of the loans it was then servicing, or approximately 40 percent. The percentage varies from time to time depending upon savings deposits and demand for mortgage money, but the ability of lenders in our area to sell part of their portfolio is very important to sustaining the economy. Loans are sold, in whole or in part, to various priviate agencies as well as to federal agencies. FHA Regulations (§203.19, C.F.R. 1971) require tax and insurance reserves in all FHA mortgages, as do Federal Regulations for all savings and loan associations on loans over 80 percent of the value of the property

(§545.6-1(a)(4)(iii), C.F.R. 1972). These types of loans average over 30 percent of defendant's volume. The policy of governmental or quasi-governmental agencies in the secondary market, such as Government National Mortgage Association, Federal National Mortgage Association and Federal Home Loan Mortgage Corporation, is and has been for many, many years to require that provision for tax and insurance reserves be in the mortgages they purchase as additional security on the mortgage, and as a result, the entire secondary market of private investors so requires. This requirement is imposed because these loans are relatively high in ratio of loan to property value, so that without the reserve, there would be risk of loss of the security through tax sale to collect the prior tax lien or through uninsured casualty loss. Hence, it is absolutely necessary for lenders in this area, in order to sustain their ability to meet demand for additional mortgage funds as required by the Intermountain economy, to have the great bulk of their portfolio of mortgages in such form as the governmental agencies in the secondary market require. In 1954, Federal National Mortgage Association, the only governmental agency then in the secondary market, required the reserves to be separately held in trust in a non-interest bearing checking account and separately accounted for. As a result, in the past 20 years, all of defendant's residential mortgages made with the expectation of potential sale of the mortgage to the secondary market, have required the borrower to pay a monthly reserve payment for future taxes and insurance. Virtually all lending institutions have similar requirements for the same reasons. (Defendant has made a limited number of mortgage loans, called "MIL" loans, for such things as home improvements, which it does not intend ever to sell to secondary markets, at substantially higher interest rates. They are not the typical residential first mortgage loans of the type herein involved. It has not in the past required reserve payments on the MIL loans. The MIL loans are not included in the statistical information herein.) Traditionally, no interest or earnings on such reserves have been paid by defendant or other savings and loan associations or financial institutions. Lenders must certify annually to all investors on loans they service that property taxes have been paid. If lenders were required to pay interest or earnings on these tax reserves, they would have no ability to collect those items on loans sold to others because loans are sold in the secondary market on the basis of a fixed, net yield to the investor after servicing expenses. Further, the ability of lenders in Utah to deal in the secondary market would be greatly jeopardized, for there is the risk that the secondary market simply would deal with the Utah mortgage lenders on more burdensome terms, and that would very seriously hurt the Utah economy. Utah lenders certainly would have to increase initial service charge fees or interest rates to compensate for the difference they would be required to pay on reserve accounts (R.281-3).

If mortgagors were entitled to interest or earnings on the reserves, who would pay it, the original mortgagee or the buyer of the mortgage? What law would set the rate, the place where the mortgage was made or where the holder resides? How could earnings be measured? Would it be earnings of the mortgagee or the holder? Would it be some percentage of his gross earnings? What if the mortgagee has earnings from various types of businesses? Even if separate investment were required for reserve funds only, lenders could only invest these reserve funds in short-term obligations which permit prompt liquidation at tax time. Would separate trust investments of reserve funds have to be made for each mortgagor? Could the reserve funds be invested for all mortgagors as a class? Is it gross interest or earnings that must be paid, or is the gross to be offset by the cost of making the investments, of receiving and accounting for the budget payments, auditing, cost of ascertainment of the correct amount of taxes and insurance premiums to pay and payment thereof, errors and omissions insurance, and the cost of reporting to mortgagors? If it is net earnings, how are the expenses to be apportioned among the lender's other expenses? The expense of handling each account would be fairly uniform, but some reserve accounts would be small so that there would be a net loss on the small accounts; if net earnings were to be paid on the larger reserve accounts, must the small reserve accounts repay the net loss on them? The contract document at bar settles none of these problems. To become entangled in these problems, and they are myriad, is to simply destroy the negotiability of existing mortgage portfolios, for no one would or could buy them if to do so would involve problems of this type. One of the main purposes of federal regulation of federal savings and loan associations is to protect the federal agency in its acquisition of mortgages and related notes from the federal savings and loan associations. Thus, great deference should be given to the federal regulations and the cases which interpret them in determining whether plaintiffs have a claim against defendant. Udall v. Tallman, 380 U.S. 1, 16-17 (1965). Those regulations all imply that plaintiffs' claim is unfounded.

Although the secondary mortgage market now requires that reserves be paid on mortgages to be purchased, consider that if mortgagees were required to pay interest or earnings on the reserves, they would either raise interest rates to compensate or, more likely, would cease collecting the reserves in instances where they were not absolutely required by law to collect such reserves. If the latter occurred, county governments would be greatly affected, for they would no longer receive a few large checks from the lending institutions on the exact day taxes are due on the many properties involved. That would increase the county's cost of receiving individual payments from the mortgagors, would impair the dependability of payments on a day certain and would increase tax delinquencies.

Consider that a mortgagee is entitled to have his security protected. He is entitled to require by contract that the borrower not waste the mortgaged premises, and that waste will be an act of default. The risk that the security will be lost or impaired through non-payment of the priority lien of property taxes or through casualty destruction is a real risk. A mortgagee is entitled to require by contract that borrowers pay property taxes and insurance premiums before they become delinquent to protect against those risks. He is entitled to require by contract that borrowers post an advance fund for payment of the taxes and insurance premiums so that the lender will have funds on hand to pay the taxes and insurance premiums as they become due. They are entitled to require such advance payments by contract, just as much as they are entitled to require a bargained-for monthly repayment of the loan and a bargained-for interest rate. Indeed, §75-5-5(a)(3), U.C.A., gives specific authority for such in providing:

> The association may require that the equivalent of . . . estimated taxes, insurance premiums and other charges . . . be paid each month in advance to the association <u>in addition to</u> interest and principal payments . . . .

The amount of the loan, the terms of repayment and the interest rate are matters of bargaining between the parties, and these are affected by, among other things, the borrower's promise to pay in advance to the lender the reserve for taxes and insurance premiums. There is nothing "unfair" about such a bargain. "No doubt the contracts . . . were 'adhesion' contracts, but we are not prepared to hold that they were unconscionable . . . ," <u>Carpenter v. Suffolk Franklin Savings Bank</u> (Mass. 1976), 346 N.E.2d 892. Now, considering that the parties have made their bargain as expressed in the contract, including the rate of interest the borrower will pay the lender on the loan and the requirement of budget payments for taxes and insurance premiums, as well as all other terms, if the parties intended the lender to pay the borrower interest or earnings on the reserve payments, which could very well affect the interest rate or other terms, would that not be expressed in the agreement? How can a mortgagor expect a court to change just that one part of the entire bargain?

Finally, just because interest rates have increased is no reason to change the bargain of the parties to say that the contract today requires interest or earnings be paid on reserves when the contract did not so require when interest rates were lower; plaintiffs' interest rate on the principal sum does not increase as general interest rates increase, and neither should the contract change as to the reserve provision. No lender would have been heard to say, in days when it cost more to handle the budget payments and keep track of the taxes and insurance premiums than he could earn on the reserves, that although there was no provision in his contract for such, he should be compensated for his loss; just because times have changed does not now permit borrowers to change the contract or claim that the contract is now unfair.

Have in mind that it undeniably benefits mortgagors, to <u>some</u> degree, to have mortgagees do the accounting work to enable a mortgagor to budget in advance for his tax and insurance bills, thereby relieving the mortgagor of the worry about not having funds to pay those large amounts when they become due, with attendant worry of the risk of uninsured destruction of his property or incurring added penalty for non-payment of taxes. Have in mind the de minimus effect on each particular mortgage.

Hence, it is clearly shown that this is not a situation

> [I]nvolving an unscrupulous loan shark attempting to hide the effective rate of a loan through deceptive rate disclosures.

> There is no ethical impropriety accompanying the practice which Plaintiffs are attempting to discredit, and this is illustrated by the fact that the United States Department of Housing and Urban Development requires maintenance of such escrow accounts for FHA insured mortgages.
>
> Moreover, there is a strong public policy which favors the practice of collecting in advance real estate taxes and insurance premiums. It extends to the borrower a useful and desirable service, much in the same manner that the Federal and state governments "withhold" taxes to insure that funds are available when the taxes become due. Defendants should not necessarily be expected to perform this service *gratis*. *Graybeal v. American Sav. & Loan Ass'n.*, 59 F.R.D. 7, 20 (D.D.C. 1973). Footnote omitted; emphasis in original.)

Rather, the present case challenges established commercial practice that has been at least tacitly approved by both Federal and state regulatory authorities for over 20 years and which has not been overturned by the legislature of this state despite ample opportunities to do so. Indeed, the statutes of Utah specifically permit the precise practice of which plaintiffs complain. All of this hardly adds up to compelling public policy that warrants the type of judicial legislation or reformation of contract that plaintiffs cry for.

There are plenty of policy reasons why federal savings and loan associations, so heavily regulated on a federal basis, should not be required to pay interest or earnings on the reserve accounts on mortgages they make in the future. Whatever view one may take as to "fairness," it is clear that the F.H.L.B.B. has left, and the courts should leave, this decision to the legislatures of the various states. The Court should do likewise in view of the new federal regulation (12 C.F.R., §545.6-11(c)), stating when interest may be paid on these escrows. The legislature can act in futuro, balancing on one hand the problem that legislation requiring compensation on reserves will put the lenders in the state at a competitive disadvantage, since they must either charge higher rates to compensate or eliminate the reserve requirements and, thus, have less secure loans to sell in the national secondary market. Against this must be balanced any conceived social good arising from the legislation. But this is a legislative problem, not a legal problem, capable of ex post facto determination by courts which must construe existing contracts, not future policy.

Having all this in mind, it is incredible to think the parties intended an implied promise in their contract that interest or earnings would be due on these budget payments. That brings us to interpretation of plaintiffs' contract.

POINT II

BORROWERS DO NOT OWN OR RETAIN ANY INTEREST IN THE RESERVE FUNDS

The monthly budget payments made by plaintiff to defendant, which are "estimated to equal" annual taxes and insurance premiums are exclusively the property of defendant under the contract. The borrowers pay monthly payments of principal, interest and budget payments. They make no payment into a specific reserve fund. Under the contract defendant "may" use the budget portion to pay taxes and insurance premiums, may apply the funds to the note, or may hold the funds as additional security. Defendant is not required to apply them to pay taxes or insurance premiums or to any special purpose, as appellants' brief suggests.

Plaintiffs do not own the funds or any res. In First Federal Savings and Loan Association of Lincoln v. The Board of Equalization of Lancaster County, 152 N.W.2d 8 (Neb. 1967), plaintiff lender challenged governmental taxation of the reserves, claiming it did not own the funds. The Court held that the funds belong to the lender:

> The borrower's only right is to require that each payment be applied in accordance with the terms of the contract. The plaintiffs are not required to keep the advance payment funds separate, but are permitted to commingle and invest them and keep the earnings . . . .
>
> . . .[T]he advance payments for insurance and taxes, when made, become the property of the plaintiffs the same as any other payment required of the borrower . . . .

Similarly, in bankruptcy proceedings, the budget payments are not the property of the debtor-mortgagor nor property which vests in the bankruptcy trustee of a bankrupt mortgagor, but rather belong to the lender; In re Simon, 167 F.Supp. 214 (E.D.N.Y. 1958). Likewise, such payments are not subject to proceedings to enforce the rights of judgment creditors of the mortgagor; Central Suffolk Hospital Association v. Downs, 213 N.Y.S.2d 192 (1961), and Valerio v. College Point Savings Bank, 48 Misc.2d 91, 264 N.Y.S.2d 343 (1965).

A few comments as to non-liability for interest on the reserves are appropriate. Since such payments belong exclusively to the lender, no implied covenant to pay interest is created, nor is the lender unjustly enriched if the payments are invested and a profit made thereon. The situation is not unique. Lessees frequently pay lessors rent in advance for the last month's rent under a lease, or tenants post advance security for cleanup at the end of tenancy, or persons post cash bonds or deposit money in checking accounts. Those situations do not typically require payment of interest or earnings on the funds paid, and the payee is entitled to commingle the funds with his own.

As a matter of general principle, 47 C.J.S., Interest, §12, page 23, says in total:

> In the absence of an agreement or custom to pay interest on money received for the use of another, one who has so

> received money to hold and pay over to the proper person generally is not chargeable with interest unless he is guilty of bad faith or unreasonable delay.
>
> One who has received money for the use of another, but is charged merely with the duty of holding the money and paying it over to the proper person, generally is not chargeable with interest unless he is guilty of bad faith or unreasonable delay in dealing with it, or unless there is an agreement to pay interest or a custom to pay interest on money so received. Where money in a person's possession is retained in good faith and without fraud or misconduct on his part, he will not be chargeable with interest for such detention.

Interest is allowable only (1) pursuant to contract, (2) for damages for wrongful detention of money, or (3) when provided by statute; 47 C.J.S., Interest, §3, page 13. No statute is here applicable. Here defendant came into possession of the funds rightfully pursuant to the contract, and no claim is made that it is wrongfully detaining the funds. Where a contract for a loan of money does not provide for interest, interest may be charged only after default in payment of the principal; Pack v. Dunn, 84 Utah 597, 37 P.2d 790. Defendant is not in default in payment thereof because defendant is entitled to hold the funds pursuant to the contract.

In all the reported cases dealing with the specific situation at bar, the courts have uniformly rejected summarily any claim for interest on the reserve funds.

Indeed, in Yudkin v. Avery Savings (Ken. 1974), 507 S.W.2d 689, the Court noted that these reserve or escrow fund cases had recently been reaching the courts with considerable frequency, and "in none of the reported cases was there found to be any obligation of the lending institution to pay interest on the escrowed money."

POINT III

UNDER NO THEORY IS DEFENDANT LIABLE FOR EARNINGS ON THE RESERVE; DEFENDANT HAS NOT BEEN UNJUSTLY ENRICHED

This case is controlled by §107(1) of the Restatements of Restitution, which provides:

> (1) A person of full capacity who, pursuant to a contract with another, has performed services or transferred property to the other or otherwise has conferred a benefit upon him, is not entitled to compensation therefor other than in accordance with the terms of such bargain, unless the transaction is rescinded for fraud, mistake, duress, undue influence or illegality, or unless the other has failed to perform his part of the bargain.

None of the exceptions apply here; plaintiffs do not claim the loan transaction should be rescinded. The terms of the bargain do not provide for any compensation as claimed by plaintiffs.

As stated in Baugh v. Darley, 184 P.2d 335 (Utah, 1947) at 337:

> Unjust enrichment of a person occurs when he has and retains money or benefits which in justice and equity belong to another.

> . . . The mere fact that a person benefits another is not of itself sufficient to require the other to make restitution therefor. Restatement of Restitution, §1, Comment C.

Schott v. Westinghouse Electric Corporation (Pa. 1969), 259 A.2d 443, held:

> The quasi-contractual doctrine of unjust enrichment is inapplicable when the relationship between the parties is founded on a written agreement of express contract.

Any interpretation of the deed of trust must begin with the document itself. The accounting for earnings on the fund is of such importance, and the manner of performing is so complex and variable, that had the parties so intended, appropriate provisions would have been included in the document. The absence of such a provision indicates the lack of such a requirement. No "implied term" as claimed by plaintiffs can be discerned from the deed of trust, nor from the action of the parties; indeed, the action of the parties is entirely to the contrary.

Plaintiffs have not cited a single case where a borrower recovered earnings on the reserve funds. Our research has not disclosed any such cases.

The great majority of courts have expressly held, on either motion to dismiss the complaint or on summary judgment, that the lender, as a matter of law, has no obligation to pay interest or earnings on the reserve funds; Zelickman v. Bell Federal Savings (Ill. 1973), 301 N.E.2d

47; Sears v. Federal Savings & Loan Assoc., 275 N.E.2d 300 (Ill. 1971); Brooks v. Valley National Bank (Ariz. 1975), 539 P.2d 958; Surrey Strathmore Corp. v. Dollar Savings Bank of New York (C.A.N.Y. 1975), 36 N.Y.2d 173, 325 N.E.2d 527; Gibson v. First Federal of Detroit, (C.A.6th 1974), 504 F.2d 826; Richman v. Security Savings & Loan Assn. (Wisc. 1973), 204 N.W.2d 511; Durkee v. Franklin Sav. Assn. (Ill. 1974), 309 N.E. 2d 118; Umdenstock v. Am. Mortgage & Investment Co. (D.C. Okla. 1973), 363 F.Supp. 1375; Manchester Gardens, Inc. v. Great West Life Assurance Co. (C.A.D.C. 1953), 205 F.2d 872; Stavrides v. Maryland National Bank (W.D.Pa. 1973), 353 F.Supp. 1972; Stavrides v. Mellon National Bank (1973), 487 F.2d 953; Yudkin v. Avery Savings (Ken. 1974), 507 S.W.2d 689; Anno. 50 A.L.R.3d 697. Other cases where borrowers have been unsuccessful on such theories as breach of contract, breach of trust, unjust enrichment, fraud, truth-in-lending, antitrust, pledgor-pledgee or agency, include: Kinee v. Abraham Lincoln Federal Savings & Loan Assn., 365 F.Supp. 975 (E.D.Pa. 1973); Tierney v. Whitestone Sav. & Loan Assn., 83 Misc.2d 855, 373 N.Y.S.2d 724 (1975); Tucker v. Pulaski Fed. Sav. & Loan Assn. (Ark. 1972), 381 S.W.2d 725; Cale v. American Nat'l Bank (1973), 370 Ohio Misc. 56; Carpenter v. Suffolk Franklin Sav. Bank (Mass. 1976), 346 N.E.2d 892.

This is an impressive body of law. All the courts have reasoned that whether a trust was intended depends upon the intent of the parties, as manifested by the contract. Most have held, even though in the contract there was no expression one way or another as to interest or earnings on the reserve, that the contract was unambiguous and did not permit recovery.

The courts have followed the language of the Restatement (Second) of Trusts, §12, Comment 1 (1959):

> Where the deposit is in escrow, that is where the money is to be paid to a third person on the happening of a designated event and in the meantime the depositor has no right to withdraw the money, it depends upon the manifestation of the intention of the parties whether the bank may use as its own the money deposited or whether the money shall be held in trust. Such a deposit ordinarily indicates an intention that the bank may use the money as its own . . . .

Zelickman, supra, is factually indistinguishable from this case. There the mortgage required the borrower:

> (3) To pay when due all taxes and assessments levied against said property or any part thereof under any existing or future law, and to deliver receipts for such payments to the Mortgagee promptly upon demand.
>
> . . .
>
> (9) To provide for payments of taxes, assessments and insurance premiums, stipulated to be paid hereunder, the Mortgagor shall deposit with the Mortgagee on each monthly payment date an amount equal to

> one-twelfth of the annual taxes and assessments levied against said premises and one-twelfth of the annual premium on all such insurance, as estimated by the Mortgagee. <u>All such deposits as made are pledged as additional security</u> for the payment of the principal mortgage indebtedness. If default is made in the payment of said deposits, the Mortgagee may, at its option, charge the same to the unpaid balance of the mortgage indebtedness and the same shall bear interest at the same rate as the principal mortgage indebtedness. As taxes and assessments become due and payable and as insurance policies expire, or premiums thereon become due, <u>the Mortgagee is authorized to use such deposits for the purpose of paying taxes</u> or assessments, or renewing insurance policies or paying premiums thereon. In the event any deficit shall exist or the deposits are so reduced that the remaining deposits together with the monthly deposits will not provide sufficient funds to pay the then current calander [sic] year's estimated taxes or the estimated insurance premium on the last day of said year, the Mortgagee may, at its option, either declare immediately due and payable or add to the unpaid balance of the mortgage indebtedness secured hereby such a sum which shall, together with the remaining deposits and monthly deposits, provide sufficient funds to pay one year's estimated taxes or insurance premiums on the last day of said year. (Emphasis added.)

That language is virtually identical to the language in the case at bar. The Court there said, in sustaining summary judgment for the lender:

> Counsel for plaintiffs . . . urge that deposits made each month by plaintiffs of sums for payment of taxes and insurance premiums, are trust funds. They predicate this contention primarily upon three key words, "deposit," "pledged" and "authorized." They urge that these deposits, being made for specific and limited purposes, become

> trust funds and that this conclusion is fortified by the pledge of the deposits, which also constitutes a trust, as well as by use of the word "authorized."
>
> . . .
>
> The complaint alleged that these monies paid to defendant by plaintiffs as tax and insurance deposits were held by defendant as a trustee or fiduciary so that defendant owed a duty to segregate the trust funds and to account to plaintiffs for earnings and profits resulting therefrom.
>
> . . .
>
> In our opinion, no express trust can be drawn from the language of the loan application or of the mortgage or from both of these documents combined. Plaintiffs covenanted to pay when due all taxes and assessments and all insurance premiums. Payment of these items thus became a primary obligation of plaintiffs with the contractual right vested in defendant to advance these items in default of payment by plaintiffs. Consequently, paragraph 9 of the mortgage above quoted should necessarily be construed simply as another security device granted expressly to defendant as mortgagee to assist it in making certain that, when the taxes and insurance premiums come due, funds will be available for their prompt payment. In no sense can the language of this instrument be construed as creating an express trust for the benefit of plaintiffs. . . .

The Court noted that while the mortgage required "deposits" "pledged" for taxes and insurance, it emphasized a number of other important elements including the need to examine and to give "meaning, life and effect" to all of the pertinent language in the legal document in question. It pointed out the absence of language requiring that the tax and insurance account be "segregated," "separated" or "isolated." It commented upon language authorizing authorizing defendant to use the deposits for payment of taxes or insurance premiums. It noted the pledge of the tax and insurance account as further security for the indebtedness due and the lack of provision for repayment of deposits. It held that even if the payments there were described as "deposits," no trust would result. It pointed out the complete lack of "a res or specific property" which "is essential for the existence of a trust." It commented upon the lack of "a segregated deposit set up solely for a specific purpose." It cited and quoted from other cases and from the regulations of the Federal Home Loan Bank Board, all of which supported the conclusion that there was no trust. In holding that as a matter of law plaintiffs could not recover under an implied trust theory, it stated that "implied trusts may be further categorized into constructive and resulting trust." It held there was no resulting trust which is generally defined and limited to situations in which land or other property is bought with the money of one person and title is taken in the name of another. It held a constructive trust arises solely by operation of law only when fraud is proved or when advantage is taken of a fiduciary relationship by the dominant party. There were no allegations in the complaint regarding fraud of any kind. It held there is no fiduciary or confidential relationship existing merely by virtue of the relationship of mortgagor and mortgagee. Plaintiffs' brief says Zelickman did not discuss plaintiffs' "pledge" theory. On the contrary, Zelickman specifically noted that plaintiff's contention was predicated on the use of the key word "pledged" and rejected it, citing Sears v. Federal Savings & Loan Assoc., 275 N.E.2d 300 (Ill.App. 1971).

In Sears, the trial court granted defendant's motion to dismiss the complaint. In affirming, the appellate court gave several reasons for its decision that the defendant was not obligated in law or equity, to account for or distribute earnings to borrowers, including:

First, defendant was not required by the contract to segregate or separate the payments from other accounts, but was merely obligated by contract to pay the insurance and taxes when due. The absence of terms requiring segregation or separation was held to show a lack of intent that a special deposit was created.

Second, the Court held:

> The monthly payments paid to defendant are not deposits in any legal sense of that term, but they are simply payments by a debtor upon amounts due the creditor.

Third, contrary to plaintiffs' contention here, the Court held every pledge does not create a trust. The Court said:

> We must expressly reject plaintiff's argument that a trust is created because of use of the word "pledge" in the note. . . . This contention is a complete oversimplification and is based upon the most elementary deductive reasoning. The syllogism is: Every pledge is a trust. This note contains a pledge. Therefore this note is a trust. However, the major premise is completely invalid. Every pledge is not a trust. Circumstances may arise in the course of any pledge situation in which some of the attributes of a trust appear; particularly with reference to management or reduction to possession of collateral. This is the type of situation which appears in the cases cited by plaintiff. . . . A pledgee who does not deal properly with property of the pledgor in his possession may be charged with fiduciary responsibility because he has become a constructive trustee or a trustee ex maleficio. However, this does not mean, and cannot mean, that every pledgee is a trustee of an express trust.
>
> It is true, as plaintiff argues, ". . . that the general property or title to the property pledged remains in the pledgor . . . ," subject to the lien or rights of the pledgee until the debt has been paid. . . . But, this merely points up and emphasizes the distinction of a pledge from the case at bar. Here, when monthly payments were made, the mortgagor divested himself of all rights to the amount paid and relied directly and solely upon the contractual obligation of defendant to pay insurance and taxes. It could be argued with greater force, and with considerably more logic, that the language, "If such sums are held in trust or carried in a borrower's tax and insurance account . . ." accentuates the absence of trust attributes from the second option because it specifically states the trust or first option as one alternative and the borrower's accounts as the second.

Fourth, even if the payments could be designated "deposits" rather than "payments," a trust to hold the funds in a special deposit was not created.

Fifth, the regulations of the Federal Home Loan Bank Board that a lender may require the monthly payments "have the force and effect of law," and "this specific regulation for advance payments by the borrower negates the idea that such payments are deposits which are to be held as a trust for the benefit of the debtor."

The case presented by plaintiffs to this Court is so similar to the Zelickman and Sears cases that the same result follows. The deed of trust, like the note in Zelickman and Sears, provides, at the option of defendant, (1) for the pledge of the budget payments as additional security; (2) withdrawal of the payments for payment of taxes and insurance; or (3) for application of the budget payments to sums due under the deed of trust. Unlike Sears, defendant here is not obligated to pay the taxes and insurance; defendant could simply hold the funds as additional security or could apply them, as additional monthly payments, to the note. Here, the deed of trust, unlike the note in Sears, makes no reference to a trust where the monthly payments would be maintained until payment of the taxes and insurance.

Both Sears and Zelickman expressly rejected plaintiffs' general theorizing about the use of the word "pledge" in this specific situation.

A deposit of money as security for the performance of a contract creates only a debtor-creditor relationship and is not a true pledge; Wilcox v. Gauntlett (Mich.), 166 N.W. 856; 72 C.J.S., Pledges §9, page 10. "[A] pledge . . . is the passing of the possession of a chattel by thereof to the pledge . . .; Campbell v. Peter, 108 Utah 565, 167 P.2d 754 (1945). None of the "pledge" cases cited in plaintiffs' brief deal with this situation here; they all involve pledges of chattels or stock.

Brooks v. Valley National Bank, supra, is the second most recent case in point, and Carpenter v. Suffolk Franklin Savings Bank (Mass. May, 1976), 346 N.E.2d 892 (Carpenter II), is the most recent. Both traced prior precedent, noting only three prior cases (including Carpenter I at 291 N.E.2d 609), which upheld borrowers' claims on a pleadings basis only. Both noted the overwhelming majority of cases denying borrower recovery as a matter of law under any theory and followed the majority. Both distinguished the three prior cases on grounds here applicable.

In Brooks, the appellate court sustained summary judgment for the lender, saying:

> [A]ll jurisdictions which have considered this problem, reaching either pro or con conclusions, have relied primarily upon the same underlying legal principles in reaching their respective conclusions.
>
> In our opinion, these agreed upon principles are:
>
> (1) That the presence or absence of words such as "in trust", "trustee" or "beneficiary" do not necessarily manifest

an intent to create a trust relationship. (Citation omitted.)

(2) Whether a trust is created depends upon the intention of the parties to be ascertained from their words, and conduct in light of the surrounding circumstances. (Citation omitted.)

(3) A debt is not a trust. Restatement 2d., Trust §12.

(4) In establishing a trust there must be a res or specific property that form the subject matters of the trust. Sears v. First Federal Savings & Loan Ass'n., supra, Bogert, Trust and Trustees, §111 (2nd Ed. 1964).

. . .[T]he mortgage in this case provides:

". . . the mortgagor, in order more fully to protect the security of this mortgage, covenants and agrees as follows:

2. That, together with, and in addition to, the monthly payments of principal and interest payable under the terms of this note secured hereby the mortgagor will pay to the mortgagee, on the 1st day of each month until the said note is fully paid, the following sums:

(a) [1/12th of the annual mortgage insurance premium required by the National Housing Act, if the note is secured under the provisions of that act.]

(b) A sum equal to [1/12 of hazard insurance premiums and taxes due], such sums to be held by mortgagor in trust to pay said . . . premiums [and] taxes . . . .

(c) All payments mentioned in the two preceding subsections of

> this paragraph and all payments to be made under the note secured hereby shall be added together and the aggregate amount thereof shall be paid by the mortgagor each month in a single payment to be applied by mortgagee to the following item in the order set forth:
>
> (I) Premium charges under contract of insurance with the Federal Housing Commissioner.
>
> (ii) Ground rents, taxes, special assessments, fire and other hazard insurance premiums [the impounds involved here],
>
> (iii) Interest on the note secured hereby; and
>
> (IV) Amortization of the principal of said note."

. . .

Looking at the cold language of the document in question it appears that the intent of the parties was that payment of impounds was made "in order more fully to protect the security of this mortgage." Consistent with this intent is the provision that failure to pay impounds will "constitute an event of default under this mortgage," leading to foreclosure of the security. It would appear that this right to foreclose upon failure to pay impounds is more compatible with a debtor-creditor relationship than with a trustee-beneficiary relationship. The mortgage also provides that these impounds in addition to being used for the payment of taxes and insurance premiums can, under certain circumstances, be used to reduce the principal indebtedness of the mortgagor. Again, this provision is inconsistent with the theory that a special res of the trust was intended to be created for the purpose of paying debts due third parties. Finally, the mortgage document provides that a lump aggregate sum is to be paid by the mortgagor and the mortgagee is given authority to allocate this single sum among various items in a descending order of priority. Such authorization is normally not afforded a trustee, because the exercise of such authority could theoretically, if the amount received was insufficient to cover all items to which payment is allocated, cause a foreclosure and thus destruction of the res of the trust.

Admittedly, that portion of the payment received by the mortgagee as impounds was intended by the parties to be used primarily for a given purpose, that is, the payment of taxes on the premises used as security for the loan and the payment of insurance premiums, insuring the premises. Does this intent to use these funds for a specific purpose create a trust relationship between the parties?

The only language in the document which could be construed as an intent to create such a trust relationship is that the mortgagee shall hold the impound "in trust." However, when we consider the conduct of the parties herein, as that conduct can be construed to relate to their intent, the mortgagee has specifically negated such an intent by its affidavit in support of the motion for summary judgment. On the mortgagor's part, Brooks' predecessor in interest for a period of more than ten years, acquiesced in the mortgagee using these funds in a manner inconsistent with a trust relationship.

Looking, then, to both the written words and the conduct of the parties, we find no factual dispute that the parties did not intend the use of the words "in trust" to create a trust relationship as to impounds. Rather, we are of the opinion, again from the language of the mortgage and from the parties' conduct, that the intent of the parties was that the Bank became contractually obligated to make the payment of taxes and insurance due on the

> mortgaged premises to the extent that the borrower made monies available to make such payment. To express this intent, they used the words "in trust." . . . This did not create a trust relationship, but merely a debtor-creditor relationship with the creditor contractually bound to use a portion of the funds received for a specific purpose. We so hold.
>
> . . .
>
> We turn now to Brooks' argument that his complaint validly stated a cause of action for "unjust enrichment". It is generally held that unjust enrichment occurs when one person has money which in justice and equity belongs to another. 66 Am.Jur.2d Restitution and Implied Contracts, §3, pg. 945. Therefore, in order for Brooks to have stated a valid cause of action against the Bank for unjust enrichment it was incumbent upon him to show that the impounds "belonged" to him. Our previous discussion dealing with the trust argument negates such an ownership interest in the impounds. We have held that the payment made by Brooks to the bank, including the amount for impounds, is in satisfaction of a debtor-creditor relationship created by the mortgage document. In satisfaction of that relationship, Brooks retains no more ownership in the funds paid as impounds than he does in the principal and interest due the Bank. What does "belong" to Brooks is a cause of action against the Bank to require it to perform its contractual obligation by paying taxes and insurance to third parties to the extent that Brooks has made funds available for this purpose.
>
> We therefore hold that payment of monthly installments to the Bank, which installments include monies for taxes and insurance are in satisfaction of a debtor-creditor relationship and upon receipt of these funds, title passes to the Bank with the corresponding contractual obligation to apply these funds in accordance with that contract.

In Carpenter II, supra the most recent case in point, the Court affirmed dismissal of the complaint after trial on the merits. The findings by the Court on trial there are no different than the undisputed facts here before the Court. It held:

> Nothing is said in the statutes or the written agreements of the parties as to interest on the payments or fruits of the investment. The general understanding and practice in Massachusetts and elsewhere over a period of some forty years has been that the bank has the right to treat the tax payments as its own. We think that a mortgagor who claims that he has made a different arrangement must have a clear understanding to that effect. See Restatement (Second) of Trusts §12, comment e (1959); 4 A. Scott, The Law of Trust §530 (3d Ed. 1967). No such showing was made.
>
> The judge ruled that neither the nature of the transaction between the plaintiffs and Suffolk Franklin nor their relationship now calls for the imposition of a resulting trust. We agree, substantially for the same reasons that we uphold his finding that there was no express trust . . . .
>
> . . . No doubt the contracts between the plaintiffs and the bank were "adhesion" contracts, but we are not prepared to hold that they were unconscionable in the aspects here in issue. . . . Customers who adhere to standardized contractual terms ordinarily "understand that they are assenting to the terms not read or not understood, subject to such limitations as the law may impose." See Restatement (Second) of Contracts §237, comment b (Tent. Drafts Nos. 1-7, 1973).

> The enrichment of the bank may have been unjust in some sense. Apparently the Legislature thought so when it enacted G.L. c. 183, §61, inserted by St.1973, c. 299, §1, effective July 1, 1975 [requires that, two years hence, interest be paid on reserves "once a year and in a manner to be determined by the mortgagee"]. But most of the unjust enrichment, if any, enriched the bank's depositors at the time. The plaintiffs do not suggest that those depositors should now disgorge their excess returns. Thus a judgment of restitution would ultimately result in a transfer of funds from present and future depositors to compensate for excess payments to past depositors. Doubtless for this reason the Legislature enacted its reform with an effective date over two years after enactment. We do not think we should go further in disrupting legitimate expectations than the Legislature was willing to go.
>
> Moreover, the statutory reform requires that interest be paid "at least once a year at a rate and in a manner to be determined by the mortgagee." We infer that the Legislature thought the amount of the banks' unjust enrichment would be very difficult to measure by any objective standards. We are not prepared to substitute our judgment on this point for that of the Legislature. In this aspect, this case is a good illustration of the advantages of legislative law reform as compared with reform by judicial decision. There was no such unjust enrichment, we hold, as to justify the imposition of a constructive trust.

In Surrey Strathmore Corp. v. Dollar Savings Bank, supra, the Court of Appeals of New York, in granting the lender's motion to dismiss, said:

> In the circumstances of the relationship between these parties it does not advance our inquiry into the determination of the rights of the mortgagor or of the obligations of the mortgagee to proceed

in reliance on categorical concepts suggested by such labels as "trust", "agency", "escrow", "debtor-creditor", for it must be evident that the relationship here does not fall essentially under any one of such classical headings or any identifiable combination of them. Reasoning predicated on such concepts would accordingly be untrustworthy. We cannot, for instance, ground any conclusion on the use of the words "in trust" in this particular mortgage clause. Resolution of the issues must depend rather on what rights and obligations the parties are found to have intended to create as manifested by the words they used in their written agreement, with parol evidence admissible to clarify ambiguities, if any, under recognized canons of construction.

Preliminarily we note that the case is before us on the Bank's motion to dismiss the petition for failure to state a cause of action. Pursuant to the provisions of CPLR 3211(c) the parties submitted affidavits and the courts below have in effect treated the motion as a motion for summary judgment. The affidavits submitted by the parties raise no issues of fact or credibility, anticipate the availability of no additional extrinsic evidence, and identify no factual inferences to be drawn from extrinsic evidence. In this circumstance then there is no occasion for fact-finding by a jury and the issue is to be determined by the court as a matter of law. (Citations omitted.)

We observe that the written expression of the agreement of the parties contains no explicit provision, one way or the other, with respect to payment of interest or earnings on the tax payments. The payment of interest or earnings was not indispensible to effectuate the objectives of the mortgage agreement and there is no other provision of the written instrument from which it may be inferred that the parties intended that there be payment of interest or earnings. Indeed, from the parties' silence the inference may be drawn that no such payment

> was intended. Even the canon of construction that a written instrument is to be interpreted against the party responsible for its draftsmanship cannot be employed conclusively to fill hiatuses in the instrument or to supply terms as to which the parties themselves omitted to make any provision. There being no express agreement of the parties and no predicate for any inference that such an agreement was intended, we conclude that this mortgagor is not entitled to the relief it now seeks.
>
> To the extent that it might be argued that the mere absence of an express provision that the mortgagor would not be entitled to any payments, in the context of the mortgagor-mortgagee relationship, creates an ambiguity as to the intention of the parties, we turn to the relevant parol evidence to resolve any such ambiguity. Here we have the undisputed proof as to what was said when the agreement was signed at the closing. [Plaintiff asked at closing if interest would be paid on reserves and was told "no.") That evidence explicitly confirms the earlier inference that no payment was intended. While it may be said that only the word "interest" was then used, in context we can only conclude that this mortgagor intended, when the question was asked and answered, to inquire whether the bank as mortgagee would make any return payment, however characterized, with respect to monies paid by the mortgagor into the tax account. The answer was a categorical "no".
>
> . . .
>
> To the extent that as a matter of public policy restrictions should be placed on the absolute freedom of either party to an agreement of the sort here involved to impose terms on the other, the issue is one for legislative address.

Plaintiffs' theory of "special bank deposits" (Point IV, appellants' brief) is answered best by <u>Durkee</u>

v. Franklin Savings Association, supra (Ill. 1974), which sustained summary judgment holding such reserve payments are not special deposits and the mortgage is not required to account for profits thereon. It held that bank deposit relationships, general or special, are contractual relationship arising from the delivery of money by the depositor to the bank, but that in the case at bar, the contractual relationship did not arise from the delivery of the first monthly reserve payment, but arose from the mortgage document wherein the borrower promised to pay the monthly reserve to the bank, that the reserve payments did not constitute deposits in the legal sense of that term and, therefore, they could not be special deposits. Of the cases plaintiffs' brief cites in support of their proposition, only Carpenter I, supra, is in point, and Durkee distinguishes Carpenter I on grounds here applicable, that in Carpenter I the Court did not have before it the mortgage document for construction.

The same reasoning which destroys plaintiffs' "special deposit" theory also applies to and destroys plaintiff's "agency" theory (Point III, appellants' brief). Plaintiffs did not pay the reserves to defendant under circumstances manifesting mutual intent that defendant would hold or use the funds subject to plaintiffs' right of control. Instead, plaintiffs paid the funds in performance of their contract so to do. Plaintiff's agency theory is wholly unsupported by any authority in this specific instance.

Only three cases give appellants any breath of hope. One is Carpenter I, supra, which Carpenter II, supra, handles. Brooks, supra, distinguished and declined to follow Carpenter I, saying:

> The Massachusetts appellate court did not have before it the mortgage document which it was alleged created the trust agreement and thus was limited to a determination of whether, if true, the allegation of the mortgagor's complaint stated a cause of action.

The same distinction may be made of appellants' second case, Buchanan v. Brentwood Fed. Svgs. & Loan Assn. (Pa. 1974), 320 A.2d 117, where judgment dismissing the complaint for failure to state a claim was reversed and the case was remanded expressly to determine the language of the mortgage:

> Reversal . . . is required because this court cannot say with assurance that the trial court considered each mortgage and bond agreement individually when it concluded that appellant could not establish in any circumstance the existence of a trust relationship.

Here, contrary to Carpenter I and Buchanan, the exact mortgage language is before the Court.

Buchanan and Carpenter are distinguishable because both cases arose upon motion to dismiss complaints which did not specifically allege the contract terms; the complaints there merely alleged in general terms the fact of the escrow payments and claimed such "created trust" or "unjustly enriched" the mortgagee and, hence, the appellate courts remanded for appropriate findings.

Abrams v. Crocker Citizens National Bank (1974), 114 Cal.Rptr. 913, is the only other case found by us or cited by plaintiffs that did not grant judgment in favor of the mortgagee as a matter of law. That case arose upon summary judgment. The appellate court noted the mortgage required the bank to "hold such . . . payments in trust to pay . . . premiums and taxes," and noted conflicting affidavits filed by the parties, the mortgagor saying he intended the reserves to be held in trust by the bank, and the bank saying it did not so intend. The Court held the intention of the parties was controlling and remanded for trial because of

> [A] factual conflict between appellant's declaration that they expected and intended the funds to be held in trust and respondent's declaration that it never intended to create a trust."

Here, the mortgage does not require the funds to be held in trust. Abrams is contrary to the other cases and is weak in any event, for really, the unexpressed subjective intent of the parties is not admissible. Here, plaintiffs filed no counter-affidavits as in Abrams. No factual conflict here exists, for plaintiffs have admitted they paid the monthly payments for 11 years without expectation that interest or earnings would be paid thereon. That admission and distinction brings us to our final point.

POINT IV

THE DOCTRINE OF PRACTIAL CONSTRUCTION SHOWS
THE PARTIES DID NOT INTEND THE CONTRACT
TO REQUIRE PAYMENT OF INTEREST OR EARNINGS
ON THE RESERVE;
SUMMARY JUDGMENT IS HERE PROPER

The deed of trust here does not expressly require defendant to pay interest nor to make an accounting of earnings. Plaintiffs claim such an obligation resulted from an "implied term." This Court has stated that "the doctrine of practical construction may be applied only when the contract is ambiguous"; Bullfrog Marina, Inc. v. Lentz, 28 U.2d 261, 501 P.2d 266 (1972). There is no ambiguity in the deed of trust -- defendant is not required to pay interest and is not required to account to plaintiffs concerning plaintiffs' budget payments; the great majority of cases stated in Point III support defendant's position as a matter of law. Should the Court consider the minority view as stated in only the Carpenter I, Buchanan and Abrams cases, then parol evidence would become admissible.

The only parol evidence here shows, without contradiction or conflict:

(1) Plaintiffs knew at the time they closed the mortgage that defendant required budget payments and

did not pay interest or earnings thereon. While plaintiffs thought this was unfair, they did not discuss the subject at closing or request any change in the contract.

(2) Plaintiffs have paid all budget payments for 11 years without expectation or request to receive any earnings on the budget payments.

Under the doctrine of practical construction, a contract may be interpreted consistent with the actions of the parties. Bullough v. Sims, 16 U.2d 304, 400 P.2d 20 (1965); Hardinge Co. v. Eimco Corp., 1 U.2d 320, 266 P.2d 494 (1954), Zeese v. Estate of Siegel, (Utah 1975), 534 P.2d 85. It is conclusively here shown that the parties did not intend any contractual obligation requiring defendant to pay interest or account for profits in connection with the budget payments.

"In the interpretation of contracts, the interpretation given by the parties themselves as shown by their acts will be adopted by the court"; Hardinge Co. v. Eimco Corp., supra, 266 P.2d at 496. See also 3 Corbin on Contracts, §558 (1960) at page 249, et seq.

In Surrey Strathmore Corp. v. Dollar Savings Bank, supra, the Court looked to the conversation between the parties at time of closing to resolve any ambiguity. The mortgagor asked if interest would be paid on the reserves and was told no. The Court, in affirming summary judgment for the bank, held that if parol evidence were admissible, that evidence would require granting summary judgment. In Carpenter II and Brooks v. Valley National Bank, supra, the Court held the same type of conduct by plaintiffs administered the coup de grace to their claims. Plaintiffs here did not ask at closing because they admittedly knew defendant would not pay interest or earnings on the reserves. That knowledge equally confirms that no question of fact here exists as to such parol evidence, and the case is, therefore, ripe for summary judgment.

Plaintiffs here may not even claim the benefit of conflicting parol evidence of intent of the parties, as in Carpenter I, Buchanan and Abrams. Here, plaintiffs not only moved for summary judgment themselves, they took the position before the trial court "that defendant is liable as a matter of law to plaintiffs upon the written contract alleged in the Amended Complaint and that parol evidence is inadmissible" (R.479). They took that position in urging their motion for summary judgment and in resisting defendant's motion. They offered no evidence or affidavits whatever except the written trust agreement. The reason plaintiffs must take such position is obvious; the parol evidence of their conduct overwhelmingly shows the parties did not intend defendant must account for earnings on the reserves. That being so, even if the Court were inclined to follow the minority Buchanan and Carpenter I cases, the result would be no different on trial.

CONCLUSION

On principle, on custom, on past practice between the parties, on plaintiffs' admitted knowledge, on obvious practical requirements of business, on the language of the particular contract pleaded, and on any theory of implied interest, trust or unjust enrichment, plaintiffs' complaint on this particular contract must fail, for upon the undisputed facts, plaintiffs may not recover as a matter of law on this contract for the relief prayed for. It is significant that not one case has held a lender must pay interest or earnings on mortgage reserves, while numerous cases have summarily held he need not, in sound, logical, authoritative decisions.

The Summary Judgment should be affirmed and defendant should be awarded its costs.

DATED this _______ day of September, 1976.

Respectfully submitted,

MOYLE & DRAPER

By ______________________________

Joseph J. Palmer
Attorney for Defendant
600 Deseret Plaza
Salt Lake City, Utah 84111

CERTIFICATE OF MAILING

I hereby certify that on the 2nd day of September, 1976, two true and correct copies of the foregoing Brief of Respondent were mailed, postage prepaid, to Robert J. DeBry, attorney for plaintiffs, 2040 East 4800 South, Salt Lake City, Utah.

____